SOAH DOCKET NO. 582-08-1700
TCEQ DOCKET NO. 2008-0091-UCR

PETITION OF RATEPAYERS APPEALING RATES ESTABLISHED BY CLEAR BROOK CITY MUNICIPAL UTILITY DISTRICT	§	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

SOAH DOCKET NO. 582-08-2863
TCEQ DOCKET NO. 2008-0093-UCR

APPEAL OF THE RETAIL WATER AND WASTEWATER RATES OF THE LOWER COLORADO RIVER AUTHORITY	§	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

SOAH DOCKET NO. 582-09-1168
TCEQ DOCKET NO. 2008-1645-UCR

PETITION OF WEST TRAVIS COUNTY MUNICIPAL UTILITY DISTRICT NO. 3 FOR REVIEW OF RAW WATER RATES	§	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

REQUEST FOR ANSWERS TO CERTIFIED QUESTIONS

Pursuant to section 80.131, title 30 of the Texas Administrative Code, this is a request from the Administrative Law Judges (ALJs) in the three referenced cases seeking answers to the questions certified herein. In each case, the ALJs have issued orders on the applicability of section 49.2122 of the Texas Water Code to three factually distinct cases involving different aspects of the Commission's jurisdiction over the ratemaking authority of districts. Section 49.2122 states in its entirety:

> ESTABLISHMENT OF CUSTOMER CLASSES. (a) Notwithstanding any other law, a district may establish different charges, fees, rentals, or deposits among classes of customers that are based on any factor the district considers appropriate, including:

(1) the similarity of the type of customer to other customers in the class, including:

(A) residential;
(B) commercial;
(C) industrial;
(D) apartment;
(E) rental housing;
(F) irrigation;
(G) homeowner associations;
(H) builder;
(I) out-of-district;
(J) nonprofit organization; and
(K) any other type of customer as determined by the district;

(2) the type of services provided to the customer class;

(3) the cost of facilities, operations, and administrative services to provide service to a particular class of customer, including additional costs to the district for security, recreational facilities, or fire protection paid from other revenues; and

(4) the total revenues, including ad valorem tax revenues and connection fees, received by the district from a class of customers relative to the cost of service to the class of customers.

(b) A district is presumed to have weighed and considered appropriate factors and to have properly established charges, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously.

TEX. WATER CODE ANN. § 49.2122 (Vernon 2008).

In all three cases, various parties have filed motions to certify questions that essentially ask whether section 49.2122 alters the TCEQ's regulatory process over district ratemaking by creating a presumption in all types of cases that a district's rates are presumed valid absent a showing that the district acted arbitrarily and capriciously. They widely disagreed on which questions to certify, and some parties filed responses asking the ALJs to deny certification of any question. Below is a list of the parties in each case and whether they support or oppose certification.

Petition of Ratepayers Appealing Rates Established by Clear Brook City Municipal Utility District, SOAH Docket No. 582-08-1700, TCEQ Docket No. 2008-0091-UCR

Clear Brook City Municipal Utility District	Supports certification
TCR Highland Meadow Limited Partnership	Supports certification
Executive Director	Supports certification
Office of Public Interest Counsel	Supports certification

Appeal of the Retail Water and Wastewater Rates of the Lower Colorado River Authority (LCRA), SOAH Docket No. 582-08-2863, TCEQ Docket No. 2008-0093-UCR

City of Bee Cave	Opposes certification
West Travis County Municipal Utility District No. 3	Opposes certification
LCRA	Supports certification
Executive Director	Supports certification
Office of Public Interest Counsel	No position at time of certification

Petition of West Travis County Municipal Utility District No. 3, SOAH Docket No. 582-09-1168, TCEQ Docket No. 3008-1645-UCR

West Travis County Municipal Utility District No. 3	Opposes certification
LCRA	Supports certification
Executive Director	Supports certification
Office of Public Interest Counsel	No position at time of certification

The ALJs have reviewed the motions and responses regarding the certification issue and agree that the motions should be granted in part. Having reviewed all of the proposed questions and seeking the Commission's interpretation of section 49.2122 on key points in these and likely future cases, the ALJs have determined that the following are the most appropriate questions to certify:

1. Is Texas Water Code section 49.2122 so inconsistent with Texas Water Code section 13.043(j) that the two statutory provisions cannot be harmonized?

2. Does Texas Water Code section 49.2122(b) create a presumption that rates set by a district are properly established absent a showing that the district action setting the rates was arbitrary and capricious?

3. Does Texas Water Code section 49.2122(b) only create a presumption that customer classes established by a district are properly established absent a showing that the district action establishing the classes was arbitrary and capricious?

4. If the answer to Question No. 2 is YES, does Texas Water Code section 49.2122(b) require the petitioner to make an initial showing that the district's rate-setting action was arbitrary and capricious?

5. If the answer to Question No. 4 is YES, in the circumstance that there is no showing that the district action setting the rates was arbitrary and capricious and the rates are therefore presumed to be "properly established," is there any further inquiry required into whether the rates themselves are valid? If so, what is the standard under which the rates themselves must be judged?

6. If the answer to Question 2 is YES, is the petitioner required to make the initial showing the district's rate-setting action was arbitrary and capricious whether the rate affected is for retail service, wholesale service, or raw water?

The ALJs hereby certify these six questions to the Commission for interpretation. Attached are the ALJs' respective orders on this issue. The ALJs have abated their cases while they await the Commission's response.

Signed May 1, 2009.

KERRIE JO QUALTROUGH
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

HENRY D. CARD
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

WILLIAM G. NEWCHURCH
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

SOAH DOCKET NO. 582-08-1700
TCEQ DOCKET NO. 2008-0091-UCR

PETITION OF RATEPAYERS APPEALING RATES ESTABLISHED BY CLEAR BROOK CITY MUNICIPAL UTILITY DISTRICT	§ § § § § §	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

ORDER NO. 6
OVERRULING SPECIAL EXCEPTIONS, DENYING IN PART AND GRANTING IN PART MOTION TO LIMIT AND FOR PROTECTION FROM DISCOVERY, GRANTING MOTION TO REVISE SCHEDULE, AND REQUIRING PARTIES TO SUBMIT REVISED CASE SCHEDULE

I. INTRODUCTION

On September 24, 2008, Clear Brook City Municipal Utility District (Clear Brook) filed special exceptions to TCR Highland Meadow Limited Partnership's (TCR's) First Amended Petition for Review. It renewed its argument that TCR has failed to plead grounds for relief, in that TCR had not pled that Clear Brook's rates are arbitrary and capricious. On September 30, 2008, based on its position that TCR must plead and prove that the rates are arbitrary and capricious, Clear Brook filed a motion for a protective order limiting the discovery that TCR seeks. Clear Brook also asked that the schedule be revised to address various concerns.

In response, TCR, on October 2, 2008, filed a Second Amended Petition, which added a claim that Clear Brook's rates are arbitrary and capricious. TCR also filed a response to Clear Brook's discovery objections, claiming that they have been rendered moot, if they ever had any validity, due to the second petition amendment.

On October 17, 2008, a pre-hearing teleconference was held to consider the above pleadings, and following appeared:

PARTY	REPRESENTATIVE
TCR	Dylan B. Russell
Clear Brook	Paul Sarahan
Executive Director (ED)	Shana L. Horton
Office of Public Interest Counsel (OPIC)	Eli Martinez

Clear Brook's special exceptions are overruled because they have been rendered moot by TCR's second amended petition. Clear Brook's motion to limit discovery and for a protective order is granted in part and denied in part.

The motion to revise the schedule is also granted. As set out below in this Order, the ALJ has changed his thinking since the October 17, 2008, teleconference and has concluded that TCR must prefile and present its direct case first. The parties should confer and by October 29, 2008, file a proposed revised schedule that takes this change and other considerations into account.

II. SPECIAL EXCEPTIONS

The parties agree that TCR's Second Amended Petition, which added a claim that Clear Brook's rates are arbitrary and capricious, has rendered moot Clear Brook's special exceptions on that point. Because they are moot, Clear Brook's special exceptions are overruled.

III. MOTION TO LIMIT AND FOR PROTECTION FROM DISCOVERY

Clear Brook argues three grounds for limiting and protecting it from the discovery that TCR seeks. The first is that the discovery should be limited to information relevant to whether it acted arbitrarily and capriciously in setting the rates about which TCR complains. The heart of this argument is Clear Brook's contention that under Water Code § 49.2121 (b) its rates are

presumed appropriate unless TCR proves that they are arbitrary and capricious. According to Clear Brook, that means that discovery should be very limited.

TCR does not agree that those are the only issues, but even if they were, TCR argues that all of the discovery that it seeks is reasonably calculated to lead to information relevant to those two issues. The ALJ agrees with TCR.

There is no dispute that Clear Brook is a general or special law district to which Chapter 49 of the Water Code applies.[1] It is also true that Water Code § 49.2122 creates a presumption in Clear Brook's favor. It reads:

> § 49.2122. ESTABLISHMENT OF CUSTOMER CLASSES.
>
> (a) Notwithstanding any other law, a district may establish different charges, fees, rentals, or deposits among classes of customers that are based on any factor the district considers appropriate, including:
>
> (1) the similarity of the type of customer to other customers in the class, including:
>
> (A) residential;
> (B) commercial;
> (C) industrial;
> (D) apartment;
> (E) rental housing;
> (F) irrigation;
> (G) homeowner associations;
> (H) builder;
> (I) out-of-district;
> (J) nonprofit organization; and
> (K) any other type of customer as determined by the district;
>
> (2) the type of services provided to the customer class;
>
> (3) the cost of facilities, operations, and administrative services to provide service to a particular class of customer, including additional costs to the district for security, recreational facilities, or fire protection paid from other revenues; and

[1] Water Code § 49.002(a).

(4) the total revenues, including ad valorem tax revenues and connection fees, received by the district from a class of customers relative to the cost of service to the class of customers.
(b) A district is presumed to have weighed and considered appropriate factors and to have properly established charges, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously.

Chapter 311 of the Government Code is the Code Construction Act.[2] It applies to the Water Code and the Commission's rules adopted under the Water Code.[3] Under the Code Construction Act, it is presumed that an entire statute is intended to be effective.[4] If a general provision conflicts with a special or local provision, the provisions shall be construed, if possible, so that effect is given to both.[5] If the conflict between the general provision and the special or local provision is irreconcilable, the special or local provision prevails as an exception to the general provision, unless the general provision is the later enactment and the manifest intent is that the general provision prevail.[6] Words and phrases in statutes and rules are to be read in context and construed according to common usage unless they have acquired a technical or particular meaning by legislative definition or otherwise.[7] Moreover, in construing a statute, the following may be considered:

(1) object sought to be attained;
(2) circumstances under which the statute was enacted;
(3) legislative history;
(4) common law or former statutory provisions, including laws on the same or similar subjects;
(5) consequences of a particular construction;
(6) administrative construction of the statute; and

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[2] Gov't Code § 311.001.

[3] Gov't Code § 311.002(1) and (4).

[4] Gov't Code § 311.021(2).

[5] Gov't Code § 311.026(a).

[6] Gov't Code § 311.026 (b).

[7] Gov't Code § 311.011(a) and (b).

(7) title (caption), preamble, and emergency provision.[8]

As its title indicates, Section 49.2122 concerns the establishment of customer classes for, as the body of the text twice indicates, "charges, fees, rentals, or deposits." Interestingly, that list of items does not specifically include water rates, like those at issue in this case. Looking in the broader context, however, water rates and services are generally governed by Chapter 13 of the Water Code. For purposes of Chapter 13, Water Code § 13.002(17) defines "rate" to mean:

> . . . every compensation, tariff, charge, fare, toll, rental, and classification or any of those items demanded, observed, charged, or collected whether directly or indirectly by any retail public utility for any service, product, or commodity described in Subdivision (23) of this section and any rules, regulations, practices, or contracts affecting that compensation, tariff, charge, fare, toll, rental, or classification.

There is enough of an overlap between that definition of "rate" and the "charges, fees, rentals, and deposits" to which Water Code § 49.2122 applies for the ALJ to conclude that the presumption contained in Section 49.2122(b) comes into play in a case like this where water rates are at issue. Moreover, the Chapter 13 definition of rate is applicable because it is Water Code § 13.043(b)(4) that authorizes TCR to bring the appeal that is the subject of this case. Water Code § 13.043(b)(4) states:

> Ratepayers of the following entities may appeal the decision of the governing body of the entity affecting their water, drainage, or sewer rates to the commission:
>
> ***
>
> (4) a district or authority created under Article III, Section 52, or Article XVI, Section 59, of the Texas Constitution that provides water or sewer service to household users; and
>
> ***

When such an appeal is brought, Water Code § 13.043 requires the Commission to ensure that the districts rate's meet certain standards. It states:

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[8] Gov't Code § 311.023.

> (e) In an appeal under Subsection (b) of this section, the commission shall . . . fix in its final order the rates the governing body should have fixed in the action from which the appeal was taken. . . .
>
> (j) In an appeal under this section, the commission shall ensure that every rate made, demanded, or received by any retail public utility or by any two or more retail public utilities jointly **shall be just and reasonable. Rates shall not be unreasonably preferential, prejudicial, or discriminatory but shall be sufficient, equitable, and consistent in application to each class of customers.** The commission shall use a methodology that preserves the financial integrity of the retail public utility. . . . (Emphasis added.)

The Commission has long had a rule, 30 TAC § 291.41(i), that restates the standards of review set out in Water Code § 13.043(j). Section 291.41(i) predates Water Code § 49.2122, which the Legislature adopted in 2007.[9] In 2008, however, the Commission amended 30 TAC § 291.41(i) to add the following sentence: "To the extent of a conflict between this subsection and Texas Water Code, §49.2122, Texas Water Code, §49.2122 prevails."[10] In adopting the amendment, the Commission stated:

> The Commission adopts this change because [Water Code] §49.2122, as amended by SB3, §7.01, 80th Legislative Session, 2007, allows a district to establish different charges, fees, rentals, or deposits among classes of customers based on any factor the district considers appropriate, including the factors listed in [Water Code] §49.2122(a), unless the district has acted arbitrarily or capriciously.[11]

It is clear from the above that the Commission has concluded that Water Code § 49.2122 applies to a water-rates appeal brought under Water Code § 13.043(b)(4) and, to the extent that there is a conflict between them, Water Code § 49.2122(b) prevails over Water Code § 13.043(j).

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[9] Acts 2007, 80th Leg., R.S., Ch. 1430, § 7.01, eff. September 1, 2007.

[10] Amended to be effective July 10, 2008, 33 TexReg 5327.

[11] 33 Tex. Reg. 5329.

Thus, TCR will need to show that Clear Brook acted arbitrarily and capriciously in order to overcome the presumption of Water Code § 49.2122(b). This leads Clear Brook to argue that discovery should be very limited and TCR is not entitled to, among other things, documents concerning:

- Communications between Clear Brook and third parties regarding Water Code § 49.2122;
- Whether Clear Brook set its rates based on the need to improve, update, construct, and maintain the system;
- The design and planning of Clear Brook's system;
- All of the services that Clear Brook provides;
- Clear Brook's revenue and expenditures from 2000 onward;
- Clear Brook's employees, officials, and contractors whose job duties relate to Clear Brook's order setting rates;
- Clear Brook's governance, especially required procedures;
- Matters considered by Clear Brook's consultant in developing the rates at issue; and
- Clear Brook's expenses, bank statements, loans, customer water usage, revenue by customer type, revenue offsets, TCEQ inspections, licenses, and orders for several years.

Clear Brook also objects to requests for documents and admissions and interrogatories that concern those and similar issues. It claims that these, too, concern matters that are not relevant to whether it acted arbitrarily and capriciously. The ALJ disagrees. He concludes that all of these discovery requests are reasonably calculated to lead to the discovery of evidence relevant to determining whether Clear Brook acted arbitrarily or capriciously in weighing or considering appropriate factors or in establishing the rates at issue. Moreover, Clear Brook is entitled to very broad discovery, since nearly all of the potentially relevant information is in the custody and control of Clear Brook and its rate consultant. Thus, the relevancy objections set out in Clear Brook's motion to limit discovery and for protection are overruled.

Clear Brook also contends that discovery should be limited to what was available to its board, which would not include documents that were obtained, used, relied on, or prepared by its

consultant who proposed the rates that Clear Brook adopted that are at issue in this case. It cites Water Code § 13.043(e) for this proposition, which states:

> The commission may consider only the information that was available to the governing body at the time the governing body made its decision and evidence of reasonable expenses incurred by the retail public utility in the appeal proceedings.

According to Clear Brook, this means that documents that its rate consultant had or considered were not available to the Board and would not be relevant. The ALJ finds that an artificial and overly constrained construction of the word "available." He concludes that Clear Brook had access to, thus control over, any documents that its rate consultant reviewed, whether members of the Board actually looked at them or not. Accordingly, they are discoverable under Texas Rule of Civil Procedure 192.3(b). This objection is also overruled.

Lastly, Clear Brook argues that TCR is not entitled to completed IRS tax forms concerning for its employees and contractors for the years 2005 through 2008. It claims these are confidential by federal law. The ALJ agrees. This objection is sustained, and TCR's requests for discovery of these tax documents are limited as requested by Clear Brook.

IV. REQUEST TO MODIFY PROCEDURAL SCHEDULE

In its motion to revise the schedule, Clear Brook argued that TCR should be required to prefile and present its direct case first because it must show, if it can, that Clear Brook acted arbitrarily and capriciously in weighing and considering appropriate factors and properly establishing rates. The ED now agrees with that argument, but TCR does not. However, all of the parties agreed at the conclusion of the October 17, 2008, teleconference that some modification of the case schedule would be necessary to take into account other developments. They asked that they be given time to develop and propose a revised case schedule.

After more careful additional consideration, the ALJ has concluded that he has been incorrect in his prior rulings concerning the order of presenting direct cases. He now agrees with Clear Brook and the ED that TCR must prefile and present its direct case first

During the prior preliminary hearing and pre-hearing conference, the ALJ concluded that Water Code § 49.2122, concerned only what is generally referred to as rate design, which concerns the allocation of a utility's cost of service among its various classes of customers. The ALJ believed that other statutes assigned to Clear Brook the burden of proving its just and reasonable cost of service, while Section 49.2122 assigned to TCR only the burden of proving that the rate design that Clear Brook chose was arbitrary and capricious. After more carefully focusing on several provisions of Water Code Chapter 13 and rethinking how they relate to Section 49.2122, the ALJ now believes that Clear Brook has no obligation to prove anything unless TCR first shows that Clear Brook acted arbitrarily and capriciously.

It is true that Water Code § 13.182 provides:

> (a) The [Commission] shall ensure that every rate made, demanded, or received by any utility or by any two or more utilities jointly shall be just and reasonable.
>
> (b) Rates shall not be unreasonably preferential, prejudicial, or discriminatory but shall be sufficient, equitable, and consistent in application to each class of consumers.

Additionally, Water Code § 13.184(c) provides:

> (c) In any proceeding involving any proposed change of rates, the burden of proof shall be on the utility to show that the proposed change, if proposed by the utility, or that the existing rate, if it is proposed to reduce the rate, is just and reasonable.

Strictly speaking, these provisions are not applicable to districts.[12] However, Water Code § 13.043(j) and 30 TAC § 291.41(i) reiterate the just, reasonable, *etc.* standards and 30 TAC §291.12 places the same burden of proof on "the provider of water and sewer services."

The terms arbitrary, capricious, just, and reasonable are not defined by the Water Code, although Water Code §§ 13.043(j) and 13.182(b) appear to give examples of characteristics that would make rates unjust or unreasonable. In common usage, something is:

- arbitrary if it exists or comes about seemingly at random or by chance or as a capricious and unreasonable act of will[13];
- capricious if it is governed or characterized by caprice, which is a sudden usually unpredictable condition, change, or series of changes[14];
- just if it has a basis in or conforms to fact or reason[15]; and
- reasonable if it is in accordance with reason and not extreme or excessive.[16]

Based on the above definitions, the ALJ sees no meaningful distinction between the words "arbitrarily" and "capriciously" or between "just" and "reasonable." He also concludes that one acts unjustly and unreasonably if one acts arbitrarily and capriciously.

It is true that Water Code § 49.2122(a) allows a district to consider a host of factors in establishing rates classes "[n]otwithstanding any other law." That does not mean that a district

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[12] Water Code § 13.181.

[13] "ARBITRARY." Merriam-Webster Online Dictionary. 2008. http://www.merriam-webster.com (October 21, 2008).

[14] "CAPRICIOUS" and "CAPRICE." Merriam-Webster Online Dictionary. 2008. http://www.merriam-webster.com (October 21, 2008).

[15] "JUST." Merriam-Webster Online Dictionary. 2008. http://www.merriam-webster.com (October 21, 2008).

[16] "REASONABLE." Merriam-Webster Online Dictionary. 2008. http://www.merriam-webster.com (October 21, 2008).

may set rates that are unjust or unreasonable to the members of any class. Water Code § 49.2122(b) provides that any rate factor, which would include a classification, and rate is presumed appropriate unless shown to be arbitrary and capricious, which is synonymous with unjust and unreasonable. Thus, when read as a whole, Water Code 49.2122 does not conflict with Water Code § 13.043(j) and 30 TAC § 291.41(i). "Notwithstanding any other law" only means that a district has broad discretion to establish rate classes, not that it may set unreasonable or unjust rates for a particular class of customers.

Based on the above, the ALJ concludes that Water Code § 49.2122(b):

- creates a presumption that Clear Brook's rates are just and reasonable;
- assigns to TCR the burden of proving that Clear Brook acted arbitrarily and capricious, which is synonymous with unjustly and unreasonably, in weighing and considering appropriate factors and properly establishing rates;
- is a later enacted statute that conflicts with 30 TAC § 291.12, concerning burden of proof, and Water Code § 49.2122(b) prevails;
- does not, nor does Water Code § 49.2122(a), conflict with Water Code § 13.043(j), which requires Clear Brook's rates to be just, reasonable, etc.; and
- relieves Clear Brook of the burden of proving that its rates are just and reasonable, which it would otherwise have under Water Code § 13.043(j) and 30 TAC §291.12, until TCR first shows that Clear Brook acted arbitrarily and capriciously.

Since TCR has the initial burden of proof, TCR should prefile and present its direct case first. Any schedule that the parties agree on should incorporate this order of presentation.

The ALJ would also note that nothing in Water Code § 49.2122 requires TCR to prove what rates Clear Brook should have set. TCR only has the limited burden of showing that Clear Brook acted in some way arbitrarily and capriciously in weighing and considering appropriate factors and properly establishing rates.

SIGNED October 22, 2008.

WILLIAM G. NEWCHURCH
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

SOAH DOCKET NO. 582-09-1168
TCEQ DOCKET NO. 2008-1645-UCR

PETITION OF WEST TRAVIS	§	**BEFORE THE STATE OFFICE**
	§	
COUNTY MUNICIPAL UTILITY	§	**OF**
	§	
DISTRICT NO. 3	§	**ADMINISTRATIVE HEARINGS**

ORDER NO. 3
SETTING OUT JURISDICTIONAL AND EVIDENTIARY DETERMINATIONS AND DENYING MOTION FOR SUMMARY DISPOSITION

I. INTRODUCTION

This proceeding involves a petition filed by the West Travis County Municipal Utility District No. 3 (MUD) under section 12.013 of the Texas Water Code[1] seeking review by the Texas Commission on Environmental Quality (TCEQ) of the rates imposed by the Lower Colorado River Authority (LCRA) for raw surface water. At the preliminary hearing, the parties disagreed on whether the evidentiary hearing should be bifurcated to first determine issues regarding the public interest. The parties also disagreed on who has the burden of proof in this proceeding. The Administrative Law Judge (ALJ) has determined that the evidentiary hearing will not be bifurcated and that the MUD bears the burden of proof as the movant. LCRA also filed a motion for summary disposition. Based on the determinations regarding TCEQ's jurisdiction and bifurcation, that motion is denied.

II. BACKGROUND

For the sole purpose of ruling on the current procedural disagreements, the ALJ accepts as true the uncontested facts asserted in the parties' briefs.

LCRA provides wholesale and retail treated water service to a large area of western Travis County and northern Hays County through the LCRA West Travis County Regional System. LCRA's source of raw water is an intake structure on Lake Austin. LCRA diverts the

[1] TEX. WATER CODE ANN. (Vernon 2008).

raw water and transports it through a transmission line to a water treatment plant. The transmission line runs through the MUD's territory prior to reaching the water treatment plant and the MUD obtains raw water from this line. The MUD is required to beneficially use this water for aesthetic purposes and for irrigation of common areas within the MUD. The MUD is the end user of this raw water and does not treat the raw water for resale.[2]

In 2002 and 2003, the MUD and LCRA entered into contracts regarding the sale and use of this raw water. Pursuant to contract, the provision of raw water from LCRA to the MUD is not considered wholesale water because the MUD does not sell the raw water to any other providers or retail customers. Furthermore, the contract specifically prohibits the MUD from reselling, conveying, giving, or transferring the raw water to any other person or entity.[3] The water is not sold for swimming or recreation or sold under a certificate of convenience and necessity.[4]

According to LCRA, the contracts provide that LCRA's board of directors may charge and collect a reasonable rate for the water provided to the MUD and that LCRA may change the rates from time to time.[5] In August 2008, LCRA's board of directors did just that and LCRA increased the price of raw water sold to its customers. The new rate went into effect on October 1, 2008. According to the MUD, prior to October 1, LCRA charged $1.10 per 1,000 gallons. After October 1, LCRA new rates were $1.90 per 1,000 gallons, an increase of $.80 per 1,000 gallons.[6]

On October 3, 2008, the MUD filed a petition with the TCEQ under section 12.013 of the Texas Water Code to review LCRA's price increase. A preliminary hearing was held on January 20, 2009. The parties disagreed on the procedural aspects of this case and a briefing schedule was developed so that the legal issues could be addressed.

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[2] LCRA's Brief on Procedural Issues, pg. 2.

[3] MUD's Initial Brief, pg. 2.

[4] LCRA's Brief on Procedural Issues, pg. 2

[5] LCRA's Brief on Procedural Issues, pg. 3.

[6] MUD's Initial Brief, pg. 2.

LCRA contends that the TCEQ does not have jurisdiction over a contract matter between two parties. In the alternative, LCRA argues that the ALJ should hold "a bifurcated trial to determine whether TCEQ has jurisdiction over the contracts between LCRA and [the MUD] as a matter of public interest."[7] The MUD contends that its petition should be heard in a single-phase hearing.[8] The Executive Director agrees that the rules LCRA relied upon, which are based on chapter 13 of the Texas Water Code, do not apply since this proceeding was brought pursuant to chapter 12 of the Texas Water Code.

The parties also dispute who has the burden of proof in this proceeding. LCRA and the ED contend that the burden is on the MUD to show not only that the rates are unjust and unreasonable, but that LCRA acted arbitrarily and capriciously as purportedly required by section 49.2122(b) of the Texas Water Code. The MUD argues that the burden of proof is on LCRA based on TCEQ rules that place the burden on the "provider of water and sewer services." The MUD provided legislative history to establish that section 49.2122(b) only applies to the establishment of classes of ratepayers, which is not an issue in this proceeding.

III. TCEQ JURISDICTION AND THE NEED FOR A BIFURCATED HEARING

The parties disagree on the course of this proceeding. After reviewing the law and the parties' arguments, the ALJ has determined that the matter will proceed to a single-phase evidentiary hearing.

LCRA's Position

LCRA argues that this matter should be dismissed because the TCEQ does not have jurisdiction to alter contracts under article I, section 16 of the Texas Constitution. In the

[7] LCRA's Brief on Procedural Issues, pg. 1. LCRA also asserts that there should be a hearing on whether the rates themselves are in the public interest. LCRA's Brief on Procedural Issues, pg. 5.

[8] MUD's Initial Brief, pg. 2.

alternative, LCRA asserts that a bifurcated hearing process should be utilized as set out in section 291.131(b), title 30 of the Texas Administrative Code (TAC).

Article I, section 16 states that "[n]o bill of attainder, ex post facto law, retroactive law or any law impairing the obligation of contracts, shall be made."[9] LCRA relies on *Texas Water Commission v. City of Fort Worth*,[10] for the proposition that there must be a hearing to determine "that the rates affected by a 'decision of the provider' adversely affect the public interest by being unreasonably preferential, prejudicial, or discriminatory."[11] LCRA asserts that subchapter I, chapter 291 of 30 TAC governs this action and requires a hearing on the public interest.

The MUD's Position

The MUD argues that this matter should be reviewed in a single-phase hearing. The MUD filed its petition under section 12.013 of the Texas Water Code. Therefore, according to the MUD, this petition is governed by section 291.44 of the TCEQ's rules. The MUD asserts that the cases and rules relied on by LCRA are distinguishable from the present case and therefore, do not require a bifurcated hearing process to first determine whether the public interest is harmed. Since the MUD filed a petition under chapter 12 of the Texas Water Code, the MUD argues that the cases relied upon LCRA to support its position are inapplicable because they concern proceedings filed under chapter 13 of the Water Code.

The ED's Position

The ED's position is similar to that taken by the MUD. A public interest hearing is not required because the rules relied on by LCRA apply only to rates for the sale of water for resale or appeals under 30 TAC § 13.043(f).[12]

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[9] TEX. CONST. art. I, § 16.
[10] 875 S.W.2d 332 (Tex. App. — Austin 1994, writ overruled).
[11] LCRA's Brief on Procedural Issues, pg. 5 (quoting, *City of Ft. Worth*, 875 S.W.2d at 336).
[12] ED's Initial Brief, pg. 5

The ALJ's Determination

The ALJ has reviewed the arguments of the parties and has determined that a bifurcated hearing process to determine the public interest is not required in this case. The law cited by LCRA does not support the proposition that a public interest hearing must be conducted in a proceeding initiated under section 12.013 of the Texas Water Code.

Section 12.013 of the Texas Water Code provides:

> (a) The commission shall fix reasonable rates for the furnishing of raw or treated water for any purpose mentioned in Chapter 11 or 12 of this code.
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> * * * *
>
> (c) The commission in reviewing and fixing reasonable rates for furnishing water under this section may use any reasonable basis for fixing rates as may be determined by the commission to be appropriate under the circumstances of the case being reviewed; provided, however, the commission may not fix a rate which a political subdivision may charge for furnishing water which is less than the amount required to meet the debt service and bond coverage requirements of that political subdivision's outstanding debt.
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> * * * *
>
> (e) The commission may establish interim rates and compel continuing service during the pendency of any rate proceeding.
>
> (f) The commission may order a refund or assess additional charges from the date a petition for rate review is received by the commission of the difference between the rate actually charged and the rate fixed by the commission, plus interest at the statutory rate. . . .

To implement section 12.013, the TCEQ has adopted rules setting out the requirements for such petitions. Section 291.44 provides:

> (a) Ratepayers seeking relief under the Texas Water Code, §§11.036-11.041 and 12.013 should include in a written petition to the commission, the following information:

(1) the petitioner's name;

(2) the name of the water supplier from which water supply service is received or sought;

(3) the specific section of the code under which petitioner seeks relief, with an explanation of why petitioner is entitled to receive or use the water;

(4) that the petitioner is willing and able to pay a just and reasonable price for the water;

(5) that the party owning or controlling the water supply has water not contracted to others and available for the petitioner's use; and

(6) that the party owning or controlling the water supply fails or refuses to supply the available water to the petitioner, or that the price or rental demanded for the available water is not just and reasonable or is discriminatory.

* * * *

(c) If the petition for relief is accompanied by the deposit stipulated in the code, the executive director shall have a preliminary investigation of allegations contained in the petition made and determine whether or not there are probable grounds for the complaint alleged in the petition. The commission may require the petitioner to make an additional deposit or execute a bond satisfactory to the commission in an amount fixed by the commission.

(d) If, after preliminary investigation, the executive director determines that probable grounds exist for the complaint alleged in the petition, the commission shall enter an order setting a time and place for a hearing on the petition.

The jurisdiction of the TCEQ to review petitions filed pursuant to section 12.013 is well established.[13] In upholding the jurisdiction of the TCEQ's predecessor agency to fix rates, the Texas Supreme Court held that section 12.013 is little changed from when it was originally

[13] *Texas Water Comm'n v. Brushy Creek Mun. Utility Dist.*, 917 S.W.2d 19 (Tex. 1996); *Texas Water Comm'n v. Boyt Realty Co. (Trinity Water Reserve)*, 10 S.W.3d 334 (Tex. App. – Austin 1993, no writ); *Texas Water Rights Comm'n v. City of Dallas*, 591 S.W.2d 609 (Tex. Civ. App.—Austin 1979, no writ); *Trinity River Authority v. Texas Water Rights Comm'n*, 481 S.W.2d 192 (Tex. Civ. App. – Austin 1972, writ ref'd n.r.e.).

enacted.[14] According to the Austin Court of Appeals in analyzing an antecedent of section 12.013:

> The rate making authority of the Commission began with its predecessor agency, the State Board of Water Engineers, in 1913 with enactment of Articles 7560, 7561, and 7562, Revised Civil Statutes of 1925, . . . brought forward as Section 5.041 of the Texas Water Code . . . effective August 30, 1971. The rate making jurisdiction was expanded in 1918 when the antecedent statute of Article 7563 was enacted to cover furnishing water for any purpose mentioned in the irrigation Act of 1917. . . . As brought forward in the Texas Water Code (Sec. 6.056) the statute empowers the Commission to ". . . fix reasonable rates for the furnishing of water for any purpose mentioned in Chapter 5 or 6 of this code."[15]

"The legislature granted the [TCEQ] broad authority in this area: 'The commission shall fix reasonable rates for the furnishing of raw or treated water for *any* purpose in Chapter 11 or 12 of [the Water Code].'"[16] The TCEQ has exercised its "broad authority" under section 12.013 by adopting section 291.44 to set out the requirements for section 12.013 appeals. Based on the express wording of section 12.013 and well-established case law, the ALJ finds that this matter should proceed and declines to find, as urged by LCRA, that the TCEQ lacks jurisdiction over the MUD's petition.

Furthermore, the ALJ declines to find that a bifurcated hearing to determine the public interest is required. LCRA relies primarily on *Texas Water Commission v. City of Fort Worth*[17] to argue that a bifurcated hearing is necessary. In that case, the Austin Court of Appeals construed the TCEQ's authority to adjust wastewater rates under section 13.043 of the Water Code.[18] The Texas Legislature adopted chapter 13 of the Texas Water Code "to protect the public interest inherent in the rates and services of retail public utilities."[19] However, the MUD chose to file its petition under section 12.013 of the Water Code. Chapter 12 was enacted by the

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[14] *Brushy Creek*, 917 S.W.2d at 21.

[15] *Trinity River Authority*, 481 S.W.2d at 195 (citations omitted).

[16] *Trinity Water Reserve*, 10 S.W.3d at 338 (emphasis in orig.).

[17] 875 S.W.2d 332 (Tex App.—Austin 1994, writ denied).

[18] *Id.* at 334.

[19] TEX. WATER CODE § 13.001(a).

legislature as part of its continuing supervision over state water and water rights issued by the Commission.[20]

The rules relied on by LCRA are also clearly distinguishable from the present case. LCRA cites to sections 291.128 through 291.138 in subchapter I, chapter 291 of 30 TAC to support its position that a bifurcated hearing is required. However, section 291.128 clearly states that "subchapter [I] sets forth substantive guidelines and procedural requirements concerning: (1) a petition to review rates charged for the sale of *water for resale* filed pursuant to Texas Water Code, Chapter 11 or 12; or (2) an appeal pursuant to Texas Water Code, *§13.043(f)* (appeal by *retail public utility concerning a decision by a provider of water or sewer service*)."[21]

The MUD's petition does not concern water for resale and was not filed under section 13.043(f) of the Water Code. As stated by LCRA, under the contracts between it and the MUD, "[t]hese contracts were entered into under the condition that MUD No. 3 would divert water from the existing raw water supply line . . . in order to obtain raw water for irrigation purposes. . . . The provision of this service by LCRA to MUD No. 3 is not considered wholesale water because it is not being sold by MUD No. 3 to any other providers or retail customers."[22] Furthermore, the MUD did not file its petition under section 13.043(f) of the Water Code. Therefore, subchapter I does not apply to the MUD's petition under the express language of section 291.128 and the subchapter I public interest hearing procedures are not required.

LCRA relies on *Canyon Regional Water Authority v. Guadalupe-Blanco River Authority*[23] for the proposition that the subchapter I rules should apply to this proceeding as well as to the proceedings specified in section 291.128. *Canyon Regional* concerned an appeal of rates under a wholesale water contract, a type of appeal recognized by section 291.128(1) as falling within the purview of subchapter I. In that case, Canyon Regional challenged the validity of the subchapter I rules and claimed that the TCEQ had exceeded its authority by requiring a public interest hearing. The court of appeals disagreed and found that the subchapter I rules

[20] *See generally, City of San Antonio v. Texas Water Comm'n*, 407 S.W.2d 752, 768 (Tex. 1966).

[21] 30 TAC § 291.28 (emphasis added).

[22] LCRA's Brief on Procedural Issues, pg. 2.

[23] 2008 Tex. App. LEXIS 8252 (Tex. App.—Corpus Christi 2008, no writ).

were clearly within the agency's authority to adopt and that there was "no compelling reason to disturb the rate-reviewing scheme that the [TCEQ] ha[d] crafted."[24] However, in this case, LCRA asks the ALJ to disturb the very same rate-reviewing scheme by going beyond the provisions in section 291.128 and expand the applicability of subchapter I to other proceedings. The rules expressly limit the applicability of subchapter I to water for resale cases and section 13.043(f) appeals. The ALJ declines to expand subchapter I to include other proceedings and will apply the TCEQ's rules as adopted.

IV. BURDEN OF PROOF

The parties disagree on who has the burden of proof in this proceeding. After reviewing the arguments of the parties, the ALJ has determined that the burden of proof is properly placed upon the MUD.

LCRA's position

LCRA argues that the MUD bears the burden of proof in this matter, and relies primarily on section 49.2122(b) of the Texas Water Code. According to LCRA, since it is a district within the meaning of section 49.2122(b), that section places the burden of proof on the MUD because "[a] district is presumed to have weighed and considered appropriate factors and to have properly established charges, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously."[25]

The MUD's position

The MUD takes the position that the burden of proof is on LCRA. The MUD argues that chapter 291 of the TCEQ's rules "govern[s] the procedures for the institution, conduct, and determination of *all water and sewer rate causes* and proceedings before the Commission."[26]

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[24] *Id.* at 19.

[25] *Id.* at 12 (quoting, TEX. WATER CODE § 49.2122(b)).

[26] MUD's Initial Brief, pg. 5 (quoting 30 TAC § 291.1) (emphasis in brief).

Since section 291.12 places the burden of proof on the provider of water and sewer services to show that the proposed rate is just and reasonable, the MUD contends that LCRA bears the burden because it is the provider of raw water to the MUD. The MUD also relies on section 80.17(b) of 30 TAC to place the burden of proof on LCRA since it is a change in water and sewer rates not governed by subchapter I of chapter 291. In response to the arguments that section 49.2122 places the burden on the MUD to show that LCRA acted arbitrarily and capriciously, the MUD responds that based on the legislative history, section 49.2122 clearly applies to the designation of customer classes.[27]

The ED's position

The ED argues that section 49.2122 is dispositive of the issue since it creates a presumption in favor of a district, LCRA in this case.[28] The ED's position is that section 291.12 regarding the burden of proof does not apply because LCRA is not a provider of water and sewer services in this case.[29]

The ALJ's determination

The MUD has the burden of proof in this matter. Section 291.12 applies to this case and states:

> In any proceeding involving any proposed change of rates, the burden of proof shall be on the provider of water and sewer services to show that the proposed change, if proposed by the retail public utility, or that the existing rate, if it is proposed to reduce the rate, is just and reasonable. *In any other matters or proceedings, the burden of proof is on the moving party.*[30]

The first sentence of section 291.12 clearly applies to a provider acting as a retail water utility. In this case, LCRA is not a provider of retail water services to the MUD. Therefore, the first sentence of section 291.12 does not apply to this proceeding. The second sentence of section

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[27] MUD's Reply Brief, pg. 2.

[28] ED's Initial Brief, pg. 6.

[29] *Id.* at pg. 5.

[30] 30 TAC § 291.12 (emphasis added).

291.12 appears to be the catch-all phrase: in any other proceeding, the burden of proof is on the moving party. This case is another "proceeding" and since the MUD is the moving party, it has the burden of proof.

The ALJ is aware that 30 TAC § 291.1 appears to limit the applicability of chapter 291 to matters under chapter 13 of the Texas Water Code and the retail utility regulatory system. Nevertheless, the TCEQ adopted section 291.44 that is within chapter 291. By its own terms, section 291.44 applies to non-chapter 13 petitions, specifically petitions filed and hearings held under chapters 11 and 12 of the Water Code. These chapter 11 and chapter 12 petitions may or may not involve retail utility matters, although they must involve matters within the TCEQ's continuing supervision of state water and water rights. Therefore, the second sentence of section 291.12 would apply to a "proceeding" conducted under section 291.44(d), even though the "proceeding" does not involve a retail utility matter.

Furthermore, placing the burden of proof on the MUD is also supported by section 80.17 of the TCEQ's rules. Section 80.17 states:

> (a) The *burden of proof is on the moving party by a preponderance of the evidence*, except as provided in subsections (b) - (d) of this section.
>
> (b) Section 291.12 of this title (relating to Burden of Proof) governs the burden of proof in a proceeding involving a proposed change of water and sewer rates not governed by Chapter 291, Subchapter I of this title (relating to Wholesale Water or Sewer Service).
>
> (c) Section 291.136 of this title (relating to Burden of Proof) governs the burden of proof in a proceeding related to a petition to review rates changed pursuant to a written contract for the sale of water for resale filed under Texas Water Code, Chapter 11 or 12, and in an appeal under Texas Water Code, § 13.043(f).
>
> (d) In an enforcement case, the executive director has the burden of proving by a preponderance of the evidence the occurrence of any violation and the appropriateness of any proposed technical ordering provisions. The respondent has the burden of proving by a preponderance of the evidence all elements of any affirmative defense asserted. Any party submitting facts relevant to the factors prescribed by the applicable statute to be considered by the commission in

> determining the amount of the penalty has the burden of proving those facts by a preponderance of the evidence. . . .[31]

None of the exceptions in subsections (b) through (d) apply to this situation. While the MUD argues that subsection (b) creates an exception, it simply refers to the burden of proof established in section 291.12. Subsection (c) and section 291.136 do not apply because this is not a water for resale case or an appeal under section 13.043(f). Since this is not an enforcement case, subsection (d) is not applicable. Therefore, the MUD must carry the burden of proof because it is the movant in this proceeding.

After establishing that the MUD has the burden of proof, the ALJ declines to rule at this point on whether the MUD must prove that LCRA acted arbitrarily and capriciously as purportedly required under section 49.2122 of the Texas Water Code. The legislative history cited by the MUD suggests that section 49.2122(b) applies only to the process of a district's designation of classes of ratepayers, which is not the situation presented in this proceeding. Nevertheless, under section 12.013, the MUD has to prove that the rates are unreasonable and the MUD must determine how it will prove up its case. It is up to the MUD to decide whether it must also prove that LCRA was arbitrary and capricious to overcome the presumption found in section 49.2122(b), should its analysis of the legislative history later be found in error.

V. MOTION FOR SUMMARY DISPOSITION

On February 13, 2009, LCRA filed a motion for summary disposition that it later amended on February 17. In its motion, LCRA argues that there is no genuine issue of any material fact and that "[t]he water rate is a contractual issue between LCRA and MUD No. 3, and the water is not re-sold to the public."[32] LCRA further states that "[t]he public is not harmed by this contractual agreement."[33] On February 27, the MUD filed a response urging the ALJ to dismiss the motion for summary disposition.[34] After reviewing LCRA's motion and the MUD's

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[31] 30 TAC § 80.17 (emphasis added).

[32] LCRA's Amendment to Motion, pg. 1.

[33] *Id.*

[34] MUD's Response Regarding the Motion, pg. 5.

response and based on the foregoing discussion in this order, the ALJ has determined that LCRA's motion for summary disposition should be denied.

VI. ORDERING PROVISIONS

Based on the determinations in this order, the parties must attempt to reach agreement on a procedural schedule for this proceeding. Therefore, it is ORDERED:

1. The parties will confer in an attempt to reach agreement on the discovery and evidentiary hearing schedule.
2. By 5:00 p.m. on April 3, 2009, the parties must submit an agreed schedule.
3. If agreement cannot be reached, each party will submit its proposed schedule by 5:00 p.m. on April 3 and the ALJ will develop the schedule and enter an order accordingly.

Signed March 23, 2009.

KERRIE JO QUALTROUGH
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

SOAH DOCKET NO. 582-08-1700
TCEQ DOCKET NO. 2008-0091-UCR

PETITION OF RATEPAYERS APPEALING RATES ESTABLISHED BY CLEAR BROOK CITY MUNICIPAL UTILITY DISTRICT	§ § § § § §	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

ORDER NO. 7
DENYING MOTION TO RECONSIDER ORDER NO. 6, DENYING MOTIONS CONCERNING LEVEL OF REQUIRED EVIDENCE, AND GRANTING MOTION TO EXTEND DEADLINE TO PROPOSE REVISED SCHEDULE

I. MOTION TO RECONSIDER

On October 23, 2008, TCR Highland Meadow Limited Partnership (TCR) filed a motion asking the Administrative Law Judge (ALJ) to reconsider a portion of Order No. 6. TCR asked that a hearing be set on its motion and argues that:

- Clear Brook City Municipal Utility District (Clear Brook), not TCR, should be required to prefile and present its direct case first;
- Clear Brook has the burden of proving its rates are just and reasonable; and
- TCR need only provide more than a scintilla of evidence that Clear Brook acted arbitrarily and capriciously in setting the rates in dispute.

On October 27, 2008, Clear Brook filed a response and asked the ALJ to hold a hearing and deny TCR's motion to reconsider and instead rule that:

- TCR must show that Clear Brook acted arbitrarily and capriciously in the adopting the rate order, and
- To meet that burden, TCR must show that there is no more than a scintilla of evidence to support Clear Brook's rate order.

When contacted by the ALJ's Assistant, the Executive Director (ED) and the Office of Public Interest Counsel (OPIC) indicated that they would not be filing responses to the motion to reconsider. The ALJ sees no reason to hold a hearing on TCR's motion, since it concerns issues of law, which the parties have thoroughly briefed. The motions for a hearing are denied.

Additionally, TCR's motion to reconsider Order No. 6 is denied. The ALJ sees no error in the portion of the Order about which TCR complains. The ALJ still concludes that TCR has the initial burden of proof and should prefile and present its direct case first because Water Code § 49.2122(b):

- creates a presumption that Clear Brook's rates are just and reasonable;
- assigns to TCR the burden of proving that Clear Brook acted arbitrarily and capricious, which is synonymous with unjustly and unreasonably, in weighing and considering appropriate factors and properly establishing rates;
- is a later enacted statute that conflicts with 30 TEX. ADMIN. CODE (TAC) § 291.12, concerning burden of proof, and Water Code § 49.2122(b) prevails;
- does not, nor does Water Code § 49.2122(a), conflict with Water Code § 13.043(j), which requires Clear Brook's rates to be just, reasonable, *etc.*; and
- relieves Clear Brook of the burden of proving that its rates are just and reasonable, which it would otherwise have under Water Code § 13.043(j) and 30 TAC §291.12, until TCR first shows that Clear Brook acted arbitrarily and capriciously.

II. LEVEL OF REQUIRED PROOF

When Order No. 6 was issued only special exceptions, a discovery dispute, and a request to modify the procedural schedule—primarily to deal with burden of proof and the order of prefiling evidence—was before him. In the current pleadings, TCR and Clear Brook more specifically ask for rulings concerning the level of proof required to meet TCR's burden of proving that Clear Brook acted arbitrarily and capriciously in setting the disputed rates. The ALJ agrees that the case will be processed more efficiently if he rules on this issue at this time.

The level-of-proof dispute largely concerns scintillas, which are tiny amounts of something. Assuming for the sake of argument that it has any burden of proof, TCR claims that it must present only a bit more than a scintilla of evidence that Clear Brook acted arbitrarily and capriciously in setting the disputed rates. On the other hand, Clear Brook contends that TCR must show that there is no more than a scintilla of evidence to support Clear Brook's rate order. Both are incorrect.

Both Parties rely on administrative law cases decided under Tex. Gov't Code § 2001.174, its statutory ancestor, similar provisions in other statues, and similar principles developed by the courts in the absence of statutes on point. Section § 2001.174 summarize all of those and states:

> If the law authorizes review of a decision in a contested case under the substantial evidence rule or if the law does not define the scope of judicial review, a court may not substitute its judgment for the judgment of the state agency on the weight of the evidence on questions committed to agency discretion but:
>
> (1) may affirm the agency decision in whole or in part; and
>
> (2) shall reverse or remand the case for further proceedings if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:
>
> (A) in violation of a constitutional or statutory provision;
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> (B) in excess of the agency's statutory authority;
>
> (C) made through unlawful procedure;
>
> (D) affected by other error of law;
>
> (E) not reasonably supported by substantial evidence considering the reliable and probative evidence in the record as a whole; or
>
> (F) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

Thus, absent legal error, a reviewing court will almost never second-guess the weight assigned to the evidence by the agency that acted in a quasi-judicial capacity and considered the evidence presented by the parties to the dispute. The deference given to the administrative adjudicator's weighing of the evidence is enormous. As the Supreme Court of Texas summarized in *Texas Health Facilities Com. v. Charter Medical-Dallas, Inc.*, 665 S.W.2d 446, 453 (Tex. 1984):

> Although substantial evidence is more than a mere scintilla, *Alamo Express, Inc. v. Union City Transfer*, 158 Tex. 234, 309 S.W.2d 815, 823 (1958), the evidence in the record actually may preponderate against the decision of the agency and nonetheless amount to substantial evidence. *Lewis v. Metropolitan Savings and Loan Association*, 550 S.W.2d 11, 13 (Tex. 1977). The true test is not whether the agency reached the correct conclusion, but whether some reasonable basis exists in the record for the action taken by the agency. *Gerst v. Nixon*, 411 S.W.2d 350, 354 (Tex. 1966). A reviewing court is not bound by the reasons given by an agency in its order, provided there is a valid basis for the action taken by the agency. *Railroad Commission v. City of Austin*, 524 S.W.2d 262, 279 (Tex. 1975). Thus, the agency's action will be sustained if the evidence is such that reasonable minds could have reached the conclusion that the agency must have reached in

> order to justify its action. *Suburban Utility Corp. v. Public Utility Commission*, 652 S.W.2d 358, 364 (Tex. 1983).
>
> The findings, inferences, conclusions, and decisions of an administrative agency are presumed to be supported by substantial evidence, and the burden is on the contestant to prove otherwise. *Imperial American Resources Fund, Inc. v. Railroad Commission*, 557 S.W.2d 280, 286 (Tex. 1977). Hence, if there is evidence to support either affirmative or negative findings on a specific matter, the decision of the agency must be upheld. *Gerst v. Goldsbury*, 434 S.W.2d 665, 667 (Tex. 1968); see also *Lewis v. Jacksonville Building and Loan Association*, 540 S.W.2d 307, 311 (Tex. 1976).

Should either TCR or Clear Brook seek judicial review of the Commission's ultimate decision in this case, Section § 2001.174 would apply. A reviewing court would defer to the Commission's weighing of the evidence.

That leads TCR to argue that it need only provide a bit more than a scintilla of evidence that Clear Brook acted arbitrarily and capriciously. The ALJ does not agree. While only a small amount of evidence is needed to support a decision by the Commission on judicial review, the Commission demands a higher level of proof from a movant in a case before it. 30 TAC § 80.17 provides

> (a) The burden of proof is on the moving party by **a preponderance of the evidence**, except as provided in subsections (b) . . .
>
> (b) Section 291.12 of this title (relating to Burden of Proof) governs the burden of proof in a proceeding involving a proposed change of water and sewer rates not governed by Chapter 291, Subchapter I of this title (relating to Wholesale Water or Sewer Service).
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> ***
>
> (Emphasis added.)

As discussed in Order No. 6, 30 TAC §291.12 places the burden of proof on "the provider of water and sewer services." However, Water Code § 49.2122 (b) preempts that rule by requiring TCR to first show that Clear Brook acted arbitrarily and capriciously. To show that, the ALJ concludes that Rule 80.17(a) applies and requires TCR to first show by a preponderance of the

evidence that Clear Brook acted arbitrarily and capriciously. A little more than a scintilla will not do.

But Clear Brook argues that the required level of proof is even higher. It points to additional cases applying Tex. Gov't Code § 2001.174[1] and claims that they show that the courts have determined that something is not arbitrary and capricious if it is supported by substantial evidence, which need be only slightly more than a scintilla of proof. This leads Clear Brook to contend that TCR must show that there is no more than a scintilla of evidence to support the rates in dispute. The ALJ does not agree.

Clear Brook's argument rips cases out of their Texas Gov't Code § 2001.174 context. In those cases, the courts were not generally determining the meaning of arbitrary and capricious. Instead, they were determining the extent of the prohibition on a reviewing court's substituting its judgment concerning the weight of the evidence for that of the agency that acted as the neutral trier of fact and weighed the evidence. In that situation, the adjudicator is entitled to extreme deference.

Clear Brook is not entitled to that extreme deference. It did not hold a contested case and was not acting as a disinterested and impartial adjudicator when it set rates. Instead, it was acting as a seller and setting prices that it would charge TCR for service. Neither Section 2001.174 nor the long-established principles that underlie it apply in that situation. It is true that Water Code § 49.2122 creates a presumption in Clear Brook's favor, but a fair reading of that statutes does not entitle Clear Brook to the same deference accorded an adjudicative agency.

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[1] *Sanchez v. Tex. State Bd. of Med. Examiners*, 229 S.W.3d 498 (Tex. App. Austin 2007, no pet.); *Reliant Energy, Inc. v. PUC*, 153 S.W.3d 174 (Tex. App. Austin 2004, review denied); *Public Utility Com. v. Gulf States Utilities Co.*, 809 S.W.2d 201, 210 (Tex. 1991); *Gerst v. Nixon*, 411 S.W.2d 350 (Tex. 1966); *Hinkley v. Tex. State Bd. of Med. Exam'rs*, 140 S.W.3d 737 (Tex. App. Austin 2004, review denied); *Montgomery Indep. Sch. Dist. v. Davis*, 34 S.W.3d 559 (Tex. 2000); *Meador-Brady Management Corp. v. Texas Motor Vehicle Comm'n*, 833 S.W.2d 683 (Tex. App. Austin 1992), rev'd on other grounds, 866 S.W.2d 593, (Tex. 1993); and *City of El Paso v. Public Util. Comm'n*, 883 S.W.2d 179, 185 (Tex. 1994).

The ALJ concludes that Clear Brook is presumed to have weighed and considered appropriate factors and to have properly established rates absent a showing by a preponderance of the evidence that Clear Brook acted arbitrarily and capriciously.

III. EXTENSION OF DEADLINE TO FILE REVISED SCHEDULE

On October 29, 2008, TCR, with the concurrence of all parties, filed a motion to extend the October 29, 2008, deadline that Order No. 6 set for the parties to propose a revised procedural schedule. TCR asked for an extension until the ALJ ruled on TCR's motion to reconsider Order No. 6. The motion to extend is granted. The Parties shall confer and propose a new schedule by November 14, 2008.

SIGNED October 31, 2008.

WILLIAM G. NEWCHURCH
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

SOAH DOCKET NO. 582-08-2863
TCEQ DOCKET NO. 2008-0093-UCR

APPEAL OF THE	§	**BEFORE THE STATE OFFICE**
RETAIL WATER AND WASTEWATER	§	
RATES OF THE LOWER COLORADO	§	**OF**
RIVER AUTHORITY	§	
	§	**ADMINISTRATIVE HEARINGS**

ORDER NO. 3

The parties have filed briefs regarding burden of proof, standard of proof, and the applicability of TEX. WATER CODE ANN. §49.2122(b) to this rate appeal. The Administrative Law Judge (ALJ) agrees with Appellants that §49.2122(b) does not require them to prove that Lower Colorado River Authority (LCRA) acted arbitrarily and capriciously in establishing the rates at issue in this proceeding. The ALJ concludes LCRA has the burden of proving its rates are just and reasonable under Chapter 13 of the Water Code and Chapter 291 of the Texas Administrative Code. The ALJ concludes that this matter should proceed to a single-phase evidentiary hearing. The parties shall attempt to establish a procedural schedule accordingly.

TEX. WATER CODE ANN. §49.2122(b) states:

Sec. 49.2122. ESTABLISHMENT OF CUSTOMER CLASSES.
(a) Notwithstanding any other law, a district may establish different charges, fees, rentals, or deposits among classes of customers that are based on any factor the district considers appropriate, including:
(1) the similarity of the type of customer to other customers in the class, including:
(A) residential;
(B) commercial;
(C) industrial;
(D) apartment;
(E) rental housing;
(F) irrigation;
(G) homeowner associations;
(H) builder;
(I) out-of-district;
(J) nonprofit organization; and

(K) any other type of customer as determined by the district;
(2) the type of services provided to the customer class;
(3) the cost of facilities, operations, and administrative services to provide service to a particular class of customer, including additional costs to the district for security, recreational facilities, or fire protection paid from other revenues; and
(4) the total revenues, including ad valorem tax revenues and connection fees, received by the district from a class of customers relative to the cost of service to the class of customers.
(b) A district is presumed to have weighed and considered appropriate factors and to have properly established charges, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously.

All the parties concede that LCRA is a "district" within the meaning of the statute. LCRA and the Executive Director contend that the plain language of subsection (b) requires a showing that LCRA acted arbitrarily and capriciously in establishing the rates that are the subject of this appeal. Consequently, they argue, the Appellants have the preliminary burden of proving those rates to have been set arbitrarily and capriciously. Only if the Appellants make such a showing would LCRA be required to prove the rates just and reasonable.

The City of Bee Cave, West Travis County MUD Nos. 3 and 5, and the Office of Public Interest Counsel (OPIC) contend, to the contrary, that Section 49.2122 applies only to the establishment of different rates among customer classes, as was the case in *Petition of Ratepayers Appealing Rates Established by Clear Brook City Municipal Utility District*, SOAH Docket No. 582-08-1700, TCEQ Docket No. 2008-0091-UCR. In that case, the ALJ's Order No. 6 concluded that Petitioners were required to make a preliminary showing that the rates were arbitrary and capricious. They contend that the statute is, at best, ambiguous, and that the legislative history plainly shows that this section was not intended to apply to general rate appeals.

The ALJ agrees with Appellants that the meaning of Section 49.2122(b) is ambiguous. Although that subsection itself does not contain the phrase "among classes of customers," it exists in the context of a section that pertains to the establishment of customer classes. Its reference to "charges, fees, rentals and deposits" is identical to the language of subsection (a), which explicitly governs differences among customer classes. That context and language raise questions concerning

the scope and meaning of that subsection. The legislative history, set out in Appellants' briefs, supports the narrower interpretation they espouse.

LCRA notes that its rate increase, as with any overall rate change, does pertain to customer classes. While technically that is true, the ALJ cannot help but think that the Legislature would more clearly explain its meaning if it intended for LCRA and other districts to be immune from any rate appeals unless they were shown to be arbitrary and capricious.

The ALJ concludes TEX. WATER CODE ANN. § 49.2122(b) does not require Appellants to prove that LCRA acted arbitrarily and capriciously in establishing the rates that are the subject of this appeal. He concludes LCRA has the burden of proving its rates to be just and reasonable. He further concludes that this matter should proceed to a single-phase evidentiary hearing.

The parties shall confer to determine an agreed procedural schedule for this proceeding. LCRA shall file that schedule by **April 7, 2009**. If the parties cannot agree, they shall file their individual schedule proposals by that date.

SIGNED March 26, 2009.

HENRY D. CARD
ADMINISTRATIVE LAW JUDGE
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AGENCY: Environmental Quality, Texas Commission on (TCEQ)

STYLE/CASE: CLEAR BROOK CITY MUNICIPAL UTILITY DISTRICT

SOAH DOCKET NUMBER: 582-08-1700

REFERRING AGENCY CASE: 2008-0091-UCR

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AGENCY: **Environmental Quality, Texas Commission on (TCEQ)**

STYLE/CASE: **LOWER COLORADO RIVER AUTHORITY**

SOAH DOCKET NUMBER: **582-08-2863**

REFERRING AGENCY CASE: **2008-0093-UCR**

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AGENCY: **Environmental Quality, Texas Commission on (TCEQ)**

STYLE/CASE: **WEST TRAVIS COUNTY MUNICIPAL UTILITY DISTRICT NO 3**

SOAH DOCKET NUMBER: **582-09-1168**

REFERRING AGENCY CASE: **2008-1645-UCR**

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REGARDING: REQUEST FOR ANSWERS TO CERTIFIED QUESTIONS

FROM: **Judge Henry Card; Judge Kerrie Qualtrough; Judge William Newchurch**

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